



Retirement *Lifestyle* Advocates

RADIO PROGRAM

Expert Interview Series

Guest Expert: Dr. A. Gary Shilling
Insight

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**Retirement Lifestyle Advocates
961 Four Mile Road, NW
Grand Rapids, MI 49544**

Phone: (866) 921-3613

Email: info@plplanners.com

Website: www.RetirementLifestyleAdvocates.com

Dennis Tubbergen:

Welcome back to RLA Radio. I'm your host, Dennis Tubbergen. Joining me once again on today's program is returning guest, Dr. A. Gary Shilling. If you're a longtime listener, you recognize Gary as a periodic guest here. And Gary publishes a newsletter that is really must reading. If you want to know what's going on in the economy and how it might affect your investments, it's titled Insight. You can learn more by visiting agaryshilling.com or by calling his office at 888-346-7444. I'll give that web address and the phone number again before the segment is over. And Gary, welcome back to the program.

Dr. Gary Shilling:

Always glad to be with you, Dennis.

Dennis Tubbergen:

So, Gary, in your Insight newsletter for July, the headline is The Top In Interest Rates May Be Near. Is the fed here going to make the decision to be more accommodative at the maybe expense of more inflation or how do you see it?

Dr. Gary Shilling:

Well, there are a couple of features there. One is, if you look at the past, the fed tightens credit. Now they work on the very short end, overnight rate called the federal funds rate. But the effects spread throughout the curve. The further away you get from where the fed is the less the effect, but there is an effect. And so that means when the fed does shift gears, it does have an effect on longer-term yields, treasury, no yields, and 30-year treasury bond yields. And that's important because the fed tightens credit, and when they do like they're doing now, they almost always precipitate a recession. There are exceptions, but very few.

Dr. Gary Shilling:

Now when the fed gets to the point where they see that they've done the deed, that they are pretty well sealed in a recession, I think that's once again going to be true, we may already be in one, then they back away. And they oftentimes shift from tightening to credit ease even before the peak of business. They, in effect, are leading it. And so that's why you do get a leading effect of interest rates throughout the yield curve spectrum. And I think that we're at the point now where you can begin to look at that for the fed, maybe later this year, early next year, but for the fed to move.

Dr. Gary Shilling:

Now the other thing that affects is that treasuries and interest rates, I really favor treasuries because they're the safest investment vehicles around. You don't have to worry about whether the company's going to go broke or the president, what he's having for breakfast. But the point is that they really are a great safe haven. And when you do get all kinds of problems in stocks and all these speculative areas, Bitcoin, cryptocurrencies, et cetera, et cetera, even so-called stablecoins, people head for the safety of treasuries.

Dr. Gary Shilling:

And that's not only Americans, but foreigners. Foreigners, our treasury yields are higher than almost any other developed country. And second with the dollar strengthening, and that's another one of our strong areas in portfolios we run, the strengthening dollar, it means that foreign investors get a what's called a translation game. In other words, if they're investing in treasuries and dollars and the dollar goes up, that means that the value in their own currencies rises as well.

Dennis Tubbergen:

Well, Gary, you had mentioned that you believe that we may be in a recession now, and certainly it appears that way. What's your forecast for how severe this recession could be?

Dr. Gary Shilling:

It could be severe. I don't think it's going to be as severe as the 2007, 2009 recession, which was really touched off by the collapse in subprime mortgages. I don't think it measures up to that, but it could be a fairly moderate recession. Now recessions are not really... They feature big declines in stocks. I mean, normally there's a so-called bear market, meaning at least 20% decline in major stock indices, like the S&P 500. But the economy itself, and we usually look at this in inflation adjusted terms, real terms it's called, real GDP, if it declines two and a half, 3%, that's a recession. You don't have double digit declines in economic activities. It's more the lack of growth than the actual decline. But I do think that we could have that.

Dr. Gary Shilling:

But I don't see great imbalances out there that need to be corrected like the subprime mortgage excesses a decade ago. But you never know. The one thing about recessions is that they do expose a lot of speculation and there has been plenty. All the money pumped down from the Federal Reserve and by the anti-COVID rounds of stimulus, and there were three big payments, checks sent to households, that money didn't go into spending on goods and

services. It went into housing, and it went into stocks, and it went into a lot of speculations. You look at all the cryptocurrencies and these other areas that really were benefiting from this. So, you don't know what's really beneath the surface there and it's going to be revealed as things start coming apart.

Dennis Tubbergen:

So, Gary, when you take a look at where stocks are, you were on probably about four months ago and said that we'd see more downside in stocks. What's your forecast now?

Dr. Gary Shilling:

I think, well, stocks are down. You look at the S&P, they're down about 20%, a little over 20%. And I think they're about halfway to the bottom. The first half is really changing the values, the price earnings ratios, if you will, the values that people put on stocks. Now the second half is the actual decline in earnings, which is the result of the recession. And, of course, we're just moving into the earning season for the second quarter earnings. We'll know a lot more in a couple of weeks on that. But I think we're sort of in the second half. And say the first half's 20%, second half 20%, total decline, I would say around 40% in the S&P 500.

Dennis Tubbergen:

So, Gary, do you see stocks reversing when the fed maybe reverses course and becomes a little bit more accommodative? It seems that the fed has really buoyed this market up over the last several years.

Dr. Gary Shilling:

Yeah. And there was this sort of concept of the fed put. In other words, a put is basically, if you buy a put, you're buying the ability to buy stocks cheaper. And the idea was there was a Greenspan put and then the Bernanke put, and the Yellen put. It didn't get that way with the current chairman, Powell. He kind of called the end of that.

Dr. Gary Shilling:

But the point is that what happens typically is that you do get the fed shifting gears, but the positive effects of that on stocks are usually then at least offset by the weakness in earnings. Or again, the first half in a decline in stocks is more the reduction in valuations with a fed tightening, interest rates rising, more expensive to hold stocks or anything else. But then the second half, things take over and you get the earnings effect. So, stocks do turn up before the end of the recession, but they don't turn up before the

start, or as the fed sometimes shifts from tightness to ease before the start of the recession.

Dennis Tubbergen:

So, Gary, when take a look at the long Treasury bond, it's had a bit of a rough go of it this year. Can I infer from your comments that you expect that that will likely reverse here soon?

Dr. Gary Shilling:

Yeah. Well, the long Treasury bonds did get beaten up. That changed a couple of weeks ago. I think we got to the point where people were beginning to realize there was going to be a serious recession and the safe haven treasury was there. But yeah, I think we may have seen the bottom on treasury prices, the peak in yields.

Dennis Tubbergen:

And we've got about three and a half minutes left in this segment. I have conversations with people in the real estate industry. And seems that about mid-May or so perhaps due to rising interest rates, the real estate market seems to be beginning to show signs of slowing. What's your forecast for housing? And would you agree-

Dr. Gary Shilling:

I think we're going to have a lot of weakness now. Nothing as severe as the subprime mortgage collapse that we saw in 2007, 2008. But you look at house prices relative to incomes, they are higher than they were back then when you had all that subprime mortgage speculation and house prices are very sensitive to interest rates. It's kind of surprising that you haven't had a turn down in residential real estate before now, but I think you've had a feeding frenzy, if you will. You've had a lot of people who sort of said, "Oh, well, housing, you can't lose money. It's going up. I don't care. I'm going to really strain so I can afford the down payment or the interest payments on a mortgage." But I think that finally got to the point where people realized that this is just not feasible. And so, we've seen this.

Dr. Gary Shilling:

And so, we could see a big climb in housing, and housing is a small sector. It's only typically about 3% of GDP, the total sum and goods of services, produced in the economy in a given timeframe. But it's so volatile. It can add or subtract a couple of percentage points to GDP. So, it, in itself, a collapse in housing itself, can constitute a recession. So, that's why it's extremely important because it's so volatile. Of course, it's volatile because

it's so highly leveraged. If somebody puts down 3% with an FHA mortgage, they've got a leverage of 33 to 1. Hey, that's a lot of leverage.

Dennis Tubbergen:

Right. Gary, just for our listeners' benefit, how long have you been publishing Insight?

Dr. Gary Shilling:

Oh gosh, we've been doing that for over 30 years.

Dennis Tubbergen:

Well, I would encourage the listeners to check it out. You can go to agaryshilling.com and learn more. You can also call Gary's office at 888-346-7444 to learn more about the Insight publication. I'll continue my conversation with Dr. A. Gary Shilling when RLA radio returns. Stay with us.

Dennis Tubbergen:

I'm Dennis Tubbergen and you are listening to RLA radio. I have the distinct pleasure of chatting once again today with my guest, Dr. A. Gary Shilling. Dr. Shilling is the publisher of the Insight newsletter. It's a terrific publication. I would encourage you to check it out. You can learn more at agaryshilling.com. You can also call Gary's office at 888-346-7444 to learn more, and I'd encourage you to do that. Gary, you know, before we jump in and talk maybe some specific sectors in the economy, where do you see inflation topping out? Have we seen the worst of it here?

Dr. Gary Shilling:

We probably have. Now inflation is picking up, the revisions tend to be on the upside. So, we may see some further big numbers. 9.1% year over year CPI was the latest one, of course. But I think that some of the factors that really pushed it up was the reopening of the economy after the COVID shutdown, the supply chain disruptions. And, of course most recently, the Russian invasion of Ukraine. That last one is still pretty much open. The previous two, reopening the economy and the supply chains, I think they are getting eased.

Dr. Gary Shilling:

Just one example. All these ships that bring goods from Asia, consumer goods, bicycles, cars, home appliances, you name it, clothing, there were 130 of those back in January that were waiting to be unloaded in the West Coast ports of Los Angeles and Long Beach. Now they've whittled that down to 30. Those goods have been actually unloaded. They've moved inland into warehouses. And a lot of them are big dregs on the market. They're

Christmas merchandise that was over-ordered, but you don't have that supply chain disruption. Quite the opposite, you got an excess of inventories now. So, I think a lot of those issues are well on their way to resolution. But it's the war in Ukraine that you obviously don't know how that's going to end up.

Dennis Tubbergen:

So, Gary, when you start looking at this economy, particularly stocks and the different sectors, and you really break this down in your July Insight newsletter, you have energy, you have maybe utilities, and then you kind of have the rest of the market. What's your forecast for energy here?

Dr. Gary Shilling:

I think we're probably going to see continued high energy prices until we get enough weakness in the economy, and I think it is mounting up to a worldwide recession, that we reduce demand. The supply side just isn't going to increase that much. The Saudis and the Russians, they want high prices. They don't want to really supply a lot more oil at reduced prices. And American frackers, they really stepped in earlier with huge increases in output, but it was a drill-baby-drill kind of motivation. But now they're backers, their lenders, banks and their stockholders are saying, "Hey, wait, we want to see some earnings. Don't drill as much. Just let some constraints on supply push up or maintain high prices."

Dr. Gary Shilling:

So, I don't think we're going to see much ease from a supply side. But it's the demand side which will be important, and if I'm right, that this is a full-blown recession, we'll see enough weakness in demand that we'll see a substantial decline in oil prices. I mean, gasoline is going to go well. It was over five bucks a gallon now. I think it's around \$4.75, something like that. Is it going to go back to \$2 a gallon? I don't know, but I think it could be a further substantial decline from here.

Dennis Tubbergen:

Gary, there's a big push, at least by some policy makers, for green energy. What's your opinion on green energy? Is that a viable solution moving ahead? Or has it got more of a political motivation at this point in your view?

Dr. Gary Shilling:

Well, the green energy, of course, is something that Biden and the administration was pushing very hard. The problem is that a lot of these technologies take time to develop not only the technology area, but the actual outputs. And in the meanwhile, if you don't have the energy, they

can't expand fast enough to fill the gap. And therefore, that's why Biden went to Saudi Arabia with hat in hand. I mean, he had really had very disparaging remarks about the Saudis and wanted to go completely green in energy. Well, what happened?

Dr. Gary Shilling:

With the disruptions and gasoline at \$5 a gallon, hey, Biden wants the Democrats to get reelected in November and you can't do that with that kind of price in gasoline. So, he's going over there trying to get the Saudis to push up production. But the idea of the green energy, those halts, it may be important, but it's starting with such a small deal. I think the renewable energy is something like 12% of the total US consumption now. It's starting from a very, very low base and it's going to be years before it's going to be big enough to really take over from fossil fuels.

Dennis Tubbergen:

So, Gary, in your July Insight newsletter... And if you're just joining us, I'm chatting today with Dr. A. Gary Shilling. He is the publisher of the Insight newsletter. You can learn more at agaryshilling.com or call his office at 888-346-7444. You talk in your July newsletter about speculative stocks continue to drop. And one prime example of that is the ARK Innovation Exchange Traded Fund that has fallen significantly. Do you think that this era of IPOs for companies that have never made a profit is now maybe becoming a bit more rational?

Dr. Gary Shilling:

Oh, yeah. I mentioned earlier, we had a lot of speculation, all this excess money created by fiscal stimulus that the money sent out and in reaction to the pandemic. And, of course, the Federal Reserve is flooding the country with money. And that's where a lot of it went. But now with the fed tightening and a lot of these great adventures just didn't work out, so we're now seeing the reverse, and a lot of these things have virtually collapsed.

Dr. Gary Shilling:

Some of these so-called stablecoins, for example, that the crypto coins were supposedly linked to hard currencies, well, it didn't turn out. They didn't. And so, they have collapsed. Bitcoin, which is sort of the poster boy for all this, has seen a huge decline. And I think there's just been so much speculation, and you're not only getting rid of the speculation, but all the great dreams that these various speculations were going to take over the world, people are being forced to face reality. So that circulation, I think, is really pretty well on the downside.

Dennis Tubbergen:

So, Gary, we haven't talked much about this today, but we've talked about it in past interviews. There's still the issue of worldwide debt is at very excessive levels. You can disagree with that assessment if you like, but how do you see this really affecting economic growth moving ahead? Do we still have a fair amount of de-leveraging that has to happen?

Dr. Gary Shilling:

Yeah, I think we do. And leveraging, it takes two. There are two sides to do it. The borrowers who want to leverage up, they see huge profits by increasing their borrow in relation to their capital investments. And, of course, the lenders who are very happy to accommodate them because they're picking up the fees and the interest payments. So, you see this as everybody is teaming up on the upside, but then you get the reverse.

Dr. Gary Shilling:

Now there's been a concern, of course, about leverage all over the place. The federal government, and that has not had a big impact, because so many people want to be in Treasury securities that there's been plenty of money to finance it. But the real problems of leverage, I think, are more in the private sector. Again, it's nothing as big or as widespread as the subprime mortgage bubble, but you certainly see it in all these cryptocurrencies, stable currencies, these various vehicles where basically they raise money, and special purpose acquisition companies, they raise money and they say, "I'll tell you later what I'm going to do with it. Give me your money now."

Dr. Gary Shilling:

And it really is very reminiscent of what happened back in some of the great speculations, South Sea Bubble, the Tulip Bubble mania, these in the 1600-1700s. But human nature doesn't change that much over time if at all, Dennis, so people keep doing the same things. And when the money is there and the gullibility is there, there's going to be speculation and it's going to come to grief, and that's what's happening now.

Dennis Tubbergen:

So, Gary, in the time we have left, share with our listeners what your favorite asset classes might be moving ahead.

Dr. Gary Shilling:

Well, I can tell you we are registered investment advisors as well as economic consultants and investment strategists. So, I can tell you exactly what we're doing now. It's really pretty simple. It's what's known as risk off. And what that constitutes is we're long on the dollar and the dollar, we mentioned this earlier, is a safe haven and it's been extremely strong, and I think it's got further to go. You look at the Euro, it's broken below par. Japanese yen is down considerably from its peak and so on versus the dollar. So, the dollar.

Dr. Gary Shilling:

The second one is commodities. We're short copper. I like copper because it goes into almost anything that's manufactured, whether it's machinery or computers or plumbing fixtures. And so, it's a very good measure of industrial production globally. And also, there's no cartel on either supplier or demand side. Oil has this supply side cartel, and that can really change things in a hurry relative to the fundamentals. So, we're short copper. We're also short stocks, the S&P 500, the overall stock market. And I think that is, as I say, it's about halfway to the bottom.

Dr. Gary Shilling:

And the final one is Treasury bonds. I mentioned that earlier. That's really the safe haven, and with the prospect of the fed down the road shifting from tightening to ease, I think we may have already seen the top in Treasury yields, the bottom end prices. So, it's those four things that really constitute the bulk of our investments.

Dennis Tubbergen:

Well, my guest today has been Dr. A. Gary Shilling. The newsletter is Insight. You can check it out at agaryshilling.com. You can also call Gary's office at 888-346-7444 to learn more. Gary, always a pleasure to catch up with you. I can't believe how quickly 24 minutes passes, but I'd love to have you back down the road. And thank you for joining us today.

Dr. Gary Shilling:

Thanks a lot, Dennis. Look forward to it.

Dennis Tubbergen:

We will return after these words.